84-16

No.

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1983

KENNETH CORY, LEO T. McCARTHY, and JESSE R. HUFF, members of the California State Lands Commission,
Appellants,

vs.

WESTERN OIL & GAS ASSOCIATION, et al.,
Appellees.

On Appeal from the United States Court of Appeals For the Ninth Circuit

JURISDICTIONAL STATEMENT

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68 pp

QUESTIONS PRESENTED

A State regulation governing the issuance of ground leases for state property includes authorization for a form of rent calculated with reference to the volume of commodities moved across the leased land by the lessee. The regulation does not prescribe rates.

1. Does the Commerce Clause of the Constitution prohibit such a form of rent, regardless of amount, if the lessee is engaged in interstate or foreign commerce?

2. If the lessee is engaged in foreign commerce, does such a form of rent constitute a tax on imports or exports, in violation of the Import-Export Clause of the Constitution?

3. If the lessee is engaged in interstate or foreign commerce, does such a form of rent constitute a duty of tonnage, in violation of the Tonnage Clause of the Constitution?

PARTIES BELOW

Appellants Kenneth Cory, Leo T. McCarthy, and Jesse R. Huff constitute the current membership of the California State Lands Commission. Appellants McCarthy and Huff are the successors in office to two former members of the Commission who were named in the complaint. Appellees, in addition to the Western Oil and Gas Association, named in the caption, are Pacific Refining Company, Atlantic Richfield Company, Exxon Corporation, Getty Oil Company, Lion Oil Company, Shell Oil Company, Standard Oil Company of California, and Union Oil Company of California.

TABLE OF CONTENTS

TABLE OF AUTHORITIES CITED

Cases

TABLE OF AUTHORITIES CITED

CASES

Statutes

Other Authorities

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JURISDICTIONAL STATEMENT

Appellants Kenneth Cory, Leo T. McCarthy, and Jesse R. Huff, members of the California State Lands Commission, appeal from the decision of the United States Court of Appeals for the Ninth Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App. A, *infra*, pp. A-1-A-13), as modified (App. B, *infra*, p. A-14), is reported at 726 F.2d 1340. The opinion of the district court (App. D, *infra*, pp. A-17-A-25) is unreported.[1]

[1]The issues of state law raised in the complaint were finally disposed of by the state court of appeal, following an abstention order by the district court. The opinion of the state court of appeal is officially reported at 105 Cal.App.3d 554, and unofficially reported at 164 Cal.Rptr. 468.

JURISDICTION

This is an action for declaratory and injunctive relief regarding a state regulation that is alleged to violate the Commerce Clause, the Import-Export Clause, and the Tonnage Clause of the United States Constitution. Federal jurisdiction exists under 28 United States Code section 1331. The judgment of the court of appeals was entered on January 13, 1984 (App. A, *infra*, pp. A-1-A-13), and a timely petition for rehearing was denied on April 6, 1984 (App. E, *infra*, p. A-26). The notice of appeal was filed in the court of appeals on April 10, 1984. (App. F, *infra*, p. A-27.) The jurisdiction of this Court is invoked under 28 United States Code section 1254(2). (See *John P. King Mfg. Co. v. City Council of Augusta* (1928) 277 U.S. 100, 102-104; *McCollum v. Board of Education* (1948) 333 U.S. 203, 206.)

CONSTITUTIONAL PROVISIONS AND REGULATION INVOLVED

1. The Commerce Clause of the United States Constitution, which provides:

> "The Congress shall have power . . . to regulate commerce with foreign nations, and among the several States, and with the Indian tribes. . . ." (U.S. Const., art. I, § 8, cl. 3.)

2. The Import-Export Clause of the United States Constitution, which provides:

> "No State shall, without the consent of Congress, lay any imposts or duties on imports or exports. . . ." (U.S. Const., art. I, § 10, cl. 2.)

3. The Tonnage Clause of the United States Constitution, which provides:

> "No State shall, without the consent of Congress, lay any duty of tonnage. . . ." (U.S. Const., art. I, § 10, cl. 3.)

4. Section 2003 of title 2 of the California Administrative Code, which sets forth the alternative types of rent that may be used for ground leases issued by the California State Lands Commission, and which provides:

"2003. Rental.

"(a) Rental for the various categories of use shall be generally as follows:

"(1) Commercial Use: An annual rental based on any one or combination of the following rental methods with a minimum rental of $250:

"(A) A percentage of annual gross income (the percentage being based on an analysis of the market for like uses and other relevant factors);

"(B) 9% of the appraised value of the leased land;

"(C) The volume of commodities passing over the lease premises.

"(2) Industrial Use: An annual rental based on any one or combination of the following rental methods with a minimum rental of $250:

"(A) 9% of the appraised value of the leased land together with 2¢ per diameter inch per lineal foot of pipelines and conduits on the leased premises;

"(B) The volume of commodities passing over the lease premises.

"(3) Right-of-Way Use: An annual rental based on any one or combination of the following rental methods with a minimum rental of $100:

"(A) 9% of the appraised value of the leased lands, together with compensation for any damage caused to such lands;

"(B) 2¢ per diameter inch per lineal foot;

"(C) The volume of commodities passing over the lease premises.

". . . . . ."

(Cal. Admin. Code, tit. 2, § 2003.)[2]

STATEMENT OF THE CASE

The California State Lands Commission (Commission) is empowered to issue ground leases for various categories of land owned by the State of California (Cal. Pub. Resources Code, §§ 6501-6509.) The land subject to lease includes upland property as well as lands beneath navigable waterways. Pursuant to statutory authorization (Cal. Pub. Resources Code, §§ 6108, 6301, 6501.2), the Commission has enacted regulations governing its leasing practices. These regulations categorize ground leases by type (e.g., commercial, industrial, right-of-way) and set forth the alternative types of rent that may be negotiated, including various forms of fixed annual rents and also variable rents, such as rents based on a percentage of gross income and rents based on the volume of commodities passing over the leased land (volumetric rent).

By amendment to its regulations in 1976, the Commission added volumetric rent to the alternative types of rent that could be employed for ground leases. The amendment authorized the use of this type of rent but did not prescribe rates. Specific rates were left to future negotiations

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[2]The full text of section 2003 and of related sections of the regulations of the State Lands Commission is set forth in Appendix G, *infra*, pages A-29-A-37. Section 2003, with immaterial revisions, is the current version of former sections 2006 and 2007, which are the sections containing the challenged provisions as originally enacted. The full text of former sections 2006 and 2007 is set forth in Appendix H, *infra*, pages A-38-A-42.

on a lease-by-lease basis. In common with the rental modes previously set forth in the regulation, the new alternative rental mode applied across the board to all types of lessees, and regardless of the nature of their business, whether intrastate or interstate.

The amendment followed extensive administrative hearings. The record made during the course of those hearings established that volumetric rent is employed in various types of ground leases by both public and private lessors, as to improved and unimproved land, and as to upland property and tide and submerged lands. With particular regard to the ground leases of local port districts, it was established that ports charge based upon the volume of commodities moved across the leased property, not only where the port provides improvements, but also in circumstances where wharves and related facilities have been constructed and are maintained by the lessee, not the lessor. (Administrative Record (A.R.), pp. 352-353, 412 (Port of San Francisco); 424-425 (Port San Luis Harbor District); pp. 909, 916, 922, 931-932, 706, 731 (Port of Long Beach).)

Among the opponents of the amendment were various oil companies, some of whom lease marine terminal sites from the Commission. These leases give the companies the right, for payment of rental, to appropriate to their exclusive use for a term of years discrete parcels of state-owned land for the construction of berthing facilities for the loading and offloading of petroleum and petroleum products.[3]

[3]Plaintiff Standard Oil Company of California, for instance, leases 33 acres of state-owned tide and submerged land adjacent to its refinery at Richmond, upon which it has constructed a wharf and connecting causeway.

Subsequent to adoption of the amendment, the plaintiff oil companies and their trade association, the Western Oil and Gas Association, filed suit in the district court, seeking a declaration that the regulation authorizing the negotiation of volumetric rent was invalid, and an injunction prohibiting the members of the Commission from demanding and collecting such rent. The complaint alleged that any such rental charges were *per se* invalid under the United States Constitution as "(a) an unlawful charge, duty or impost on imports; (b) an undue burden and unlawful charge upon interstate commerce; and (c) an unlawful duty on tonnage."

The complaint also presented issues of state law, alleging that the regulation was contrary to a state leasing statute, and that the regulation was "unreasonable, arbitrary and capricious." Following an abstention order by the district court, these state law issues were finally determined adversely to the plaintiff companies. (*Western Oil & Gas Assn. v. State Lands Com.* (1980) 105 Cal.App.3d 554 [164 Cal.Rptr. 468].)

Upon return of the case to the district court, the parties filed cross-motions for summary judgment on the remaining federal constitutional issues. The question presented was the *per se* validity under the Constitution of the type of volumetric rent authorized by the Commission's regulation, regardless of amount.[4] The district court gave judg-

[4]At oral argument on the motions, plaintiffs' counsel framed the issue as follows: "To us what this case is about is just the validity of a throughput charge *per se*, whether the State can charge even one-millionth of [a mill] as a throughput fee." (Reporter's Transcript, p. 12.) Neither in their pleadings nor in their moving papers did plaintiffs ask that particular volumetric rents that had been negotiated for specific leases be declared invalid, although there were references to alleged high rates of return on some leases.

ment for the plaintiffs. It rejected as inapposite the State's argument that volumetric rent was a commonly-used and reasonable form of rent and thus permissible under the Commerce Clause (App., *infra*, p. A-22.) The court also denied any applicability of this Court's cases concerning exemption of the States from the Commerce Clause when they act as "market participants", concluding that "there is no analogous competitive marketplace involved in this case." (App., *infra*, p. A-23.) Finally, it rejected the State's contention that neither the Import-Export Clause nor the Tonnage Clause was applicable to ground rents. (App., *infra*, pp. A-23-A-24.) The court determined that a volumetric land rental, without the provision of additional services and facilities by the State, constituted the type of "trade barrier" that the Commerce, Import-Export, and Tonnage Clauses were "collectively" intended to prevent, and that such a rental "places a burden on interstate and foreign commerce that cannot be justified under the facts of this case." (App., *infra*, p. A-24.)

The district court entered judgment enjoining the Commission "from assessing and collecting rent based upon the volume of commodities in interstate and foreign commerce passing over tidal and submerged lands in reliance upon California Administrative Code §§ 2005(b)(2) and 2005 (b)(3)."[5] (App., *infra*, p. A-24.)

On appeal, the court of appeals affirmed, concluding that the regulation authorizing the negotiation of volumetric rent was barred by the Commerce Clause and the Import-Export Clause. (App. *infra*, p. A-13.) In reaching its con-

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[5]Currently Cal. Admin. Code, tit. 2, §§ 2003(a)(2) and 2003 (a)(3). (See App., *infra*, pp. A-33-A-34.)

clusion under both constitutional provisions, the court relied on the decisions of this Court invalidating certain types of taxes. The court did not reach plaintiffs' Tonnage Clause contention.

On the Commerce Clause issue, the court rejected the State's argument that the regulation authorized a reasonable form of rent, given the common use of this form of rent in the rental market generally. Instead, it concluded that the case was governed by Supreme Court cases concerning "user taxes", citing cases such as *Evansville Airport v. Delta Airlines* (1972) 405 U.S. 707. (App., *infra*, pp. A-8-A-9.) In so doing, it rejected the application of this Court's cases distinguishing taxes from rent charged for the private appropriation of particular parcels of public property. Applying the "user tax" cases, it concluded that volumetric rent for unimproved land necessarily yielded rentals "disproportionate to the benefits conferred by the State," that such rents were "not directed toward compensating the State for the use of the land" or the "wear and tear" from the use of the land, and that there was "no sufficient relation between the measure employed and the extent of the use of the state property." (App., *infra*, pp. A-8-A-9.) The court also rejected the State's alternative contention that, as but one "market participant" in the negotiation of ground leases, both for upland property and tide and submerged lands,[6] the Commission was not subject to the strictures of the Commerce Clause.

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[6]There are many competing lessors of upland property. And as the court recognized (App., *infra*, p. A-6), ownership and administration of tide and submerged lands is divided among the State, local government entities, and private interests. Over 60 cities, counties, and districts hold state legislative grants of tide and submerged land. (E.g., Cal. Stats. 1913, ch. 317, p. 605 (Port of

On the Import-Export Clause issue, the court adopted a similar rationale. Having determined that "there is no correlation between the volumetric rates and benefits conferred by the State," it concluded that the State "is 'levying . . . on citizens of other States by taxing goods merely flowing through their ports to the other states not situated as favorably geographically.'" (App., *infra*, pp. A-12-A-13.)

THE QUESTIONS ARE SUBSTANTIAL

The court of appeals concluded that the Commerce and Import-Export Clauses[7] completely foreclose use by the States of volumetric rental—regardless of amount—when leasing unimproved land to lessees engaged in interstate or foreign commerce. In so holding, the court employed decisions of this Court from the tax field that have no application to the issue at hand, and at the same time ignored other decisions of this Court which establish that the States are entitled to ask reasonable rent of those in interstate or foreign commerce who wish to appropriate public property to their exclusive use in furtherance of

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Richmond); Cal. Stats. 1968, ch. 1333, p. 2554 (Port of San Francisco); Cal. Stats. 1911, ch. 654, p. 1254 (Port of Oakland); Cal. Stats. 1911, ch. 656, p. 1256 (Port of Los Angeles); Cal. Stats. 1911, ch. 676, p. 1304 (Port of Long Beach).) In addition, nearly 100,000 acres of tide and submerged lands are in private ownership pursuant to one or another statutory sales program. (See Taylor, Patented Tidelands: A Naked Fee? (1972) 47 State Bar J. 420, 421; *City of Berkeley v. Superior Court* (1980) 26 Cal.3d 515, 526 [162 Cal.Rptr. 327, 606 P.2d 362].)

[7]The court of appeals did not reach plaintiffs' assertion that volumetric rent is barred as well by the Tonnage Clause. Because the district court reached this additional contention, and decided it adversely to the Commission, the Tonnage Clause question is included among those presented by this case, in order that this Court may render a fully-dispositive decision.

such commerce. The court also ignored the common use of volumetric rental by lessors generally—including both local ports and these very plaintiffs—in connection with ground leases for unimproved land.

The question is an important one. The decision of the court of appeals invalidates over 30 ground leases issued by the State Lands Commission. Further, its rationale undermines the time-honored practice whereby public ports receive for the use of port land—both improved and unimproved—payments that are calculated by reference to a per-unit charge for the various types of commodities that cross over port lands. The public ports that make these volumetric charges are subject to the same constitutional strictures as are the States. (See, e.g., *Guy v. Baltimore* (1879) 100 U.S. 434.)

I. THE COURT OF APPEALS MISAPPLIED AND DISREGARDED DECISIONS OF THIS COURT, AND SO REACHED THE WRONG CONCLUSION

The court of appeals did not dispute that the Commission had a reasonable basis in accepted ground lease rental practice for authorizing use of the challenged form of rent. Nor did it satisfactorily explain why, if the rental form could be employed regarding lessees engaged in intrastate commerce (as the state court of appeal had previously held), it could not also be employed regarding lessees engaged in interstate or foreign commerce. The decision was not grounded on a determination that the Commission had employed the rental mode in a way that discriminated against interstate or foreign commerce. Nor did the deci-

sion rest on asserted abuses in the form of unreasonably high rents; in fact, the court ignored the Commission's expressed willingness to defend the reasonableness of particular rents, should they be challenged in any future court proceedings. Finally, the court did not point to a single actual adverse impact of this form of rent on interstate or foreign commerce.

Instead, the decision was based on the completely abstract premise that *any* volumetric rent negotiated by the Commission would, ipso facto, constitute an unreasonable burden on interstate and foreign commerce and a "tax" on imports. The court's sweeping prohibition finds no basis in the decisions of this Court, and in fact conflicts with Supreme Court precedent.

A. Volumetric Rent Is Constitutionally Permissible

The court of appeals necessarily conceded that the State has a "right to the reasonable rental value of its property." (App., *infra,* pp. A-6, A-8.) It is established that interstate or foreign commerce is not entitled to a subsidy by the States; it "must pay its own way." (See *Ott v. Mississippi Barge Line* (1949) 336 U.S. 169, 174; *Western Live Stock v. Bureau* (1938) 303 U.S. 250, 254.) A venerable line of precedent makes clear that a State may obtain compensation for services rendered or property provided, even though the cost of conducting interstate or foreign commerce is thereby increased. (E.g., *Cooley v. Board of Wardens* (1851) 53 U.S. (12 How.) 299, 315-320 (pilotage); *Atlantic & Pacific Tel. Co. v. Philadelphia* (1903) 190 U.S. 160, 162-163 (cost of supervising telegraph company's local operations); *Transportation Co. v. Parkersburg* (1882)

107 U.S. 691, 701-702 (wharfage); *St. Louis v. Western Union Telegraph Co.* (1893) 148 U.S. 92, 97-98 (rent for space occupied by telegraph poles).) In the words of this Court:

> "Reasonable charges for the use of *property, either on water or land,* are not an interference with the freedom of transportation between the States secured under the commercial power of Congress. [Citations omitted.] That freedom implies exemption from charges other than such as are imposed by way of compensation for the use of the *property employed,* or for facilities afforded for its use. . . ." (Emphasis added.) (*Gloucester Ferry Co. v. Pennsylvania* (1885) 114 U.S. 196, 217.)

Contrary to the suggestion of the court of appeals (App., *infra,* pp. A-2, A-9), no constitutional principle narrowly limits the type of rent that States may employ in leasing their property solely to fixed rents derived from the leased land's fee value. Under the decisions of this Court, such charges may take various forms, including charges which, were they imposed as taxes, divorced from the conferral of specific property rights, would be prohibited by the Constitution. (See *Transportation Co. v. Parkersburg, supra,* 107 U.S. at pp. 698-699 (charge for use of a public wharf graduated by vessel tonnage "is rent charged by the owner of the property for its temporary use," therefore not a duty of tonnage proscribed by the Tonnage Clause); accord, *Packet Co. v. Keokuk* (1877) 95 U.S. 80, 84-85, 87.)

The constitutional test is simply whether the form of rent used is a reasonable one[8] and is non-discriminatory. The Commission's volumetric rental mode meets both tests.

Concerning reasonableness, this form of rent is well-grounded in accepted ground lease practices. The extensive administrative record compiled before the Commission during the hearings on the proposed amendment established that volumetric rental is commonly employed in ground leases (1) regarding all types of commodities, (2) as to both improved and unimproved land, (3) by both private and public lessors, and (4) regarding lessees engaged in interstate and foreign commerce as well as those

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[8]Although the Commission has defended the volumetric form of rent as *per se* reasonable and therefore permissible under the Commerce Clause, the Commission also maintains that its status as but one participant in the market for ground leases of the type sought by plaintiff companies for marine terminal sites frees it, as well as its public and private competitors, from application of the Commerce Clause. (See *South-Central Timber Development, Inc. v. Wunnicke* (1984) ... U.S. ..., 104 S.Ct. 2237; *White v. Massachusetts Council of Const. Employers* (1983) ... U.S. ..., 103 S.Ct. 1042; *Reeves, Inc. v. Stake* (1980) 447 U.S. 429; *Hughes v. Alexandria Scrap Corp.* (1976) 426 U.S. 794.) The court of appeals rejected this argument, erroneously focusing on but one of several situations in which volumetric rent may be negotiated, i.e., upon *renewal* of a lease where the primary term has expired. In that circumstance, the court said, the Commission has a "monopoly" on the only terminal site adjacent to the company's refinery, and is therefore the only participant in the relevant "market". (App., *infra*, pp. A-5-A-6.) The court ignored that *initial entry* into such leases is entirely discretionary on the part of both the State and the company and that, by contract, future renewal terms can be determined at the outset of the lease. Further, the lease contracts of the Commission expressly provide that any changed rentals upon renewal after expiration of the primary term must be reasonable in amount. The courts are available to resolve any disputes on this score. The court of appeals erred on this point as well.

engaged in intrastate commerce. With particular regard to the plaintiff oil companies, it was established that they are already paying such rent to local ports for leases of unimproved port property (*ante*, p. 5), and that they themselves charge rent of their retail service station lessees based upon the gallons of gasoline pumped on the leased property.[9]

Nor was there any contention below that the challenged regulation, either on its face or in its application, discriminates against these plaintiffs or against interstate or foreign commerce.[10] Indeed, the Commission has employed the volumetric type of rent authorized by the regulation regarding lessees who are neither oil companies nor en-

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[9]In addition to the numerous examples of volumetric rent adduced at the hearings before the Commission, such a form of rental is sufficiently common to warrant extensive discussion in a practice book prepared by the California Continuing Education of the Bar. (Grenert, Ground Lease Practice (Cal.Cont.Ed.Bar 1971), §§ 1.40, 1.41, 2.12-2.14 (discussing variable rent leases based on gross sales as well as "gallonage" rentals of the type used by the plaintiff companies in leasing service station sites).) The Commission follows the practice outlined in this book, deriving a minimum rent that is a percentage of the land's appraised fee value, then applying this minimum against the amounts accruing under the variable rent provisions of the lease. (Clerk's docket item 26, Horn Affidavit, pp. 5-6.)

[10]The decision of the court of appeals did, however, seem to be impliedly based on a perceived *potential* for abuse in the particular context of renegotiation of rent upon renewal of an existing lease for a marine terminal site adjacent to an existing refinery. (See App., *infra*, p. A-6.) Apart from the fact that initial lease contracts can and do remove such potential (see *ante*, fn. 8), such a potential, even if it existed, would be no basis for invalidating a particular form of rent. If bargaining power is indeed unequal, *any* form of rent lends itself to "exaction" of exorbitant compensation by the lessor. Such a perceived potential is not a basis for

gaged in interstate or foreign commerce. (Clerk's docket item 26, Horn Affidavit, pp. 3-4.)

Accordingly, because the challenged form of rent has both a reasonable basis in accepted practice in the ground lease rental market and because it is not employed in a discriminatory fashion, there was no basis for the Ninth Circuit's decision invalidating a regulation that merely authorized its use. If particular rents had been deemed unreasonable, a different question might be presented here; but the reasonableness of particular rents was not an issue below. The court determined that such rents were, *per se*, proscribed by the Constitution.

B. In Negotiating Ground Lease Rental, the States Are Not Limited to Recovery of Their Out-of-Pocket Costs

Where the court of appeals erred was in adopting the apparent premise that, in issuing ground leases to those engaged in interstate or foreign commerce, the States are limited to recoupment of their out-of-pocket costs. Its conclusion under both the Commerce Clause and the Import-Export Clause is grounded on its determination that "there is no correlation between the volumetric rates and benefits conferred by the State. . . ." (App., *infra*, pp. A-9, A-12.) What is apparently meant by this is that a State's rental mode, to survive constitutional scrutiny, must be designed to recover only the costs incurred by the State in making the leased property available for lease and maintaining it for that purpose. The court refers to the "com-

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denying to the State a form of rent that is in common use by others. The State stands ready to justify the reasonableness of rents renegotiated upon lease renewals, should such a challenge be made in future litigation.

pensating" nature of the charge, and cites a "user tax" case, *Evansville Airport v. Delta Airlines* (1972) 405 U.S. 707, 715, for the proposition that the "charge on [a] state-provided facility must be designed to help defray its cost." (App., *infra*, p. A-9.) And it adverts to cases involving "user taxes" directed at those making transient use of state highways (*McCarroll v. Dixie Lines* (1940) 309 U.S. 176; *Interstate Transit, Inc. v. Lindsey* (1931) 283 U.S. 183, noting critically that volumetric rents do not vary depending on the " 'wear and tear' from use of the land." (App., *infra*, p. A-9.) In applying this cost-recoupment test, the court found it dispositive that "the lands leased to plaintiffs are unimproved and . . . no services or facilities are provided by the State in conjunction with the lease." (*Ibid.*)

The court misapprehended the applicability of the "user tax" cases. Historically, it appears that "user taxes" were developed in response to early cases of this Court that prohibited "direct" application of general revenue taxes to those engaged in interstate commerce.[11] User taxes were accordingly fashioned to narrowly limit their revenue purpose to recouping state out-of-pocket costs incurred in providing services or facilities that directly benefitted interstate businesses. The cases concerning such taxes have no application to garden-variety ground leases whereby a lessee appropriates to his own exclusive use discrete parcels of state property. In fact, this Court in

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[11]These formalistic distinctions in the tax field have since been abandoned by the Court. (See *Commonwealth Edison Co. v. Montana* (1981) 453 U.S. 609; *Complete Auto Transit v. Brady* (1977) 430 U.S. 274; cf. *Michelin Tire Corp. v. Wages* (1976) 423 U.S. 276 (Import-Export Clause).)

Evansville Airport, supra, distinguished between the user tax on transient airport use there at issue and the rent paid by the shops, restaurants, parking concessions, and other "business" users of the airport. (405 U.S. at p. 718.) Ground leases may employ a variety of rental modes, in none of which is the rent limited solely to what is necessary to recoup the lessor's out-of-pocket costs in providing and leasing the property. Rental under variable rent leases is not so limited, and neither is rental under the nonvariable fixed rent leases endorsed by the court of appeals here.

Neither is it significant that the State does not provide services or facilities in addition to raw land. Variable rent leases recognize intensity of use of the leasehold—with or without improvements—as an accepted measure of rental value. The gallonage rent which these plaintiffs charge their own retailers for ground leases is a conspicuous example. Whether the State provides a wharf in addition to the underlying land may go to the amount of the volumetric rate, but not to the propriety of the rental mode itself.[12] Local ports charge volumetric rent for the use of unimproved port land on which the lessees, not the ports, construct wharves; and even where ports do provide a wharf, their volumetric charges exceed what is necessary to obtain a return on the improvements alone, indicating that a volumetric charge is being made on the underlying land as well.[13]

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[12]In fact, the volumetric rents that have actually been negotiated under particular leases have been substantially less in amount than the volumetric charges of local ports. (Clerk's docket item 26, Horn Affidavit, p. 7.)

[13]*Id.*, exh. 1 to Horn Affidavit, p. 9.

The conclusion of the court of appeals that volumetric rent is a "tax" proscribed by the Import-Export Clause in circumstances where the State does not provide "services or facilities" in addition to land proceeds solely and directly from its flawed Commerce Clause analysis, discussed above. Its conclusion on this ground is therefore erroneous for the same reasons. In addition, the court's conclusion on this point completely disregards the clear-cut distinction drawn in numerous cases of this Court between payments made as rent to the States as owners of real property and payments demanded by them solely by virtue of their attempts, as sovereigns, to impose prohibited forms of taxes. (See *St. Louis v. Western Union Telegraph Co.* (1893) 148 U.S. 92, 97-98; *Transportation Co. v. Parkersburg* (1882) 107 U.S. 691, 698-699; *Packet Co. v. Keokuk* (1877) 95 U.S. 80, 84-85.)

II. THE QUESTIONS ARE IMPORTANT

Appellants submit that the decision of the court of appeals is so demonstrably wrong as to warrant summary reversal by this Court. At minimum, the decision represents such an apparent misapplication and disregard of Supreme Court precedent that plenary consideration by this Court is necessary, particularly given the importance of the questions both to the State and to local public ports.

The decision invalidates over 30 existing leases of the State Lands Commission. If left standing, the decision will compel the State, now and into the indefinite future, to subsidize the commercial operations of certain of its lessees, because it forecloses use by the State of a type of variable ground lease rent in common use by other lessors,

and by these same plaintiffs, both as lessors and as lessees of local ports. In situations where this widely-accepted volumetric mode of rent would yield a higher rental than other rental modes, the State will be denied the fair rental value of its property.

Further, if the narrow view expressed in the Ninth Circuit's decision is correct, then it is not just the State's rental mode that is constitutionally flawed. Public ports make charges for use of their lands based upon amounts per unit of commodity that are specified in port tariffs or in individual ground leases. These charges of the ports are specifically *not* tied to reimbursement for the cost of providing various other port services or facilities, but are made solely for the use of particular land which may or may not be improved with a wharf provided by the port; ofttimes it is the lessee, not the port, who constructs the wharf on the subject property. And where a wharf is provided, volumetric revenues exceed what is necessary to defray the costs to the port of constructing and maintaining the wharf. Since the ports also ask these charges of persons engaged in interstate or foreign commerce, the decision here renders the local ports vulnerable to constitutional challenges of the type erroneously sustained against the State in this case. (See *Guy v. Baltimore* (1879) 100 U.S. 434.)

CONCLUSION

For these reasons, this Court should either summarily reverse, or note probable jurisdiction and set the case for plenary consideration.

July 3, 1984.

Respectfully submitted,

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Appendix A

In the United States Court of Appeals
For the Ninth Circuit

No. 82-4261
D.C. No. Civ. S-76-513

For Publication
Western Oil and Gas Association, et al.,
Plaintiffs-Appellees,

vs.

Kenneth Cory, et al.,
Defendants-Appellants.

[Filed Jan. 13, 1984]

Appeal from the United States District Court
for the Eastern District of California
Philip C. Wilkins, District Judge, Presiding
Argued and submitted January 11, 1983

OPINION

Before: TANG and ALARCON, Circuit Judges, and TAYLOR,* District Judge.

TANG, Circuit Judge.

The California State Lands Commission ("Commission") and its members appeal from the district court's grant of summary judgment in favor of plaintiffs, eight oil companies and their trade association, the Western Oil and Gas Association. The court below overturned as unconstitutional the regulations promulgated by the Commission that compute "rent" for the leasing of state-owned tidelands and

*Honorable Fred M. Taylor, District Judge for the District of Idaho, sitting by designation.

submerged lands based on the volume of oil in interstate and foreign commerce passing over the leased property. We agree that the regulations violate both the Commerce Clause and the Import-Export Clause of the United States Constitution and affirm.

I. BACKGROUND

In 1953 Congress enacted the Submerged Lands Act, 43 U.S.C. §§ 1301-1343. The Act conveyed to the States title to the land underlying the nation's harbors and seas from the high tide mark to the three-mile limit. In California, the State Lands Commission administers the tidelands and submerged lands and is authorized to lease property upon terms it deems to be in the best interest of the State. Cal. Pub. Res. Code §§ 6216, 6301, 6501-6509.

Plaintiffs own and operate several refineries on the California coast adjacent to the State lands. It is uncontested that "[p]etroleum substances must enter or depart from the facilities through a system of pipelines. Due to the physical and practical immobility of plaintiffs' processing plants, the pipelines must traverse tidal and submerged lands owned by the State." *Western Oil and Gas Ass'n v. Cory,* No. S-76-513, slip op. at 1 (E.D. Cal. Apr. 15, 1982).

Prior to April 28, 1976, the Commission leased the lands for a flat annual rate of six percent of the appraised value of the land. Thereafter, the Commission amended the regulations to allow for an alternative rental calculation based on the volume of commodities passing over the state-owned lands. The new volumetric rate, also known as a throughput charge, was codified in 2 Cal. Admin. Code § 2005 (current version at § 2003):

2005. Payment of Rentals.

(a) ....

(b) Rental Rate Schedule: The following rates shall apply to the classifications listed below:

...

(2) *Industrial Use:* The rental may be based on eight percent (8%) per annum of the appraised value of leased land together with 1½ cents per diameter inch per lineal foot for pipelines and conduits within the leased premises; and/or *an annual rental, with a specified minimum, based upon the volume of commodities passing over State land.* The minimum rental under either of these alternative rentals shall not be less than $550 per annum.

(3) *Right of Way Use:* Eight percent (8%) per annum of the appraised land value, together with damages, if any; and/or for pipelines and conduits, 1½ cents per diameter inch per lineal foot per annum, or, in lieu of either of the foregoing, *an annual rental, with a specified minimum based upon the volume of commodities passing over State land.* The minimum rental under any of the above alternatives shall not be less than $100 per annum (emphasis added).

The regulations do not set specific volumetric rates, but leave these rates subject to negotiation upon renewal of individual leases. Since the regulations were adopted, the Commission has, with each lease renewal, appraised the land, set a minimum annual rent of eight percent of the appraised value, and added an additional charge based on the volume of commodities passing over the leased land.

In September 1976, plaintiffs commenced the present action challenging the validity of the volumetric charges

under the Commerce Clause, the Import-Export Clause and the Duty of Tonnage Clause of the United States Constitution. Plaintiffs also contended that the charges violated a variety of state laws. The district court stayed the federal proceedings to allow for litigation of the state law issues in the California courts. The Sacramento County Superior Court subsequently upheld the volumetric rates and the decision was affirmed on appeal. *Western Oil and Gas Ass'n v. California State Lands Comm'n,* 105 Cal. App. 3d 544, 164 Cal. Rptr. 468 (1980).

In 1981, the parties returned to federal district court seeking adjudication of the federal constitutional claims. The trial court held that the volumetric throughput charge placed a burden on interstate and foreign commerce and that the assessments violated the Commerce, the Import-Export and the Duty of Tonnage Clauses. The court therefore granted Western Oil's motion for summary judgment and enjoined the Commission from assessing and collecting rent based on the volume of commodities in interstate and foreign commerce passing over tide and submerged lands. The Commission appeals timely.[1]

II. COMMERCE CLAUSE

The Commerce Clause provides that Congress has the power "To regulate Commerce . . . among the several States . . . ." U.S. Const. art. I, § 8, cl. 3. It is a limitation upon the power of the States and reflects the Framers' concern that the tendencies of the States towards economic Balkanization had to be avoided. *Hughes v. Oklahoma,* 441 U.S.

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[1]The district court granted, for good cause, the Commission's "protective motion" for retroactive extension of time for filing a notice of appeal pursuant to Fed. R. App. P. 4(a)(5).

322, 325-26 (1979); *Freeman v. Hewit,* 329 U.S. 249, 252 (1946). Under the Clause, "[a] State is . . . precluded from taking any action which may fairly be deemed to have the effect of impeding the free flow of trade between States." *Id.*

A. *Applicability of the Commerce Clause*

It is undisputed that up to 95% of the petroleum substances entering the oil companies' facilities are of foreign origin and that between 46-98% of the products leaving the refineries are channeled into interstate and foreign commerce. There is, therefore, no question that plaintiffs' activities are carried out in interstate commerce. *See, e.g., Maryland v. Louisiana,* 451 U.S. 725, 755-56 (1981); *Michigan Wisconsin Pipe Line Co. v. Calvert,* 347 U.S. 157, 169-70 (1954).

The State contends, however, that its leasehold activities fall outside the reach of the Commerce Clause, because it carries on a proprietary function when it leases tide and submerged lands. Moreover, the State maintains that it is merely one of many participants in the market competing for leases.

When a state acts as a market participant, rather than a market regulator, it is said to act in a proprietary capacity and is not subject to the limitations of the Commerce Clause. *See White v. Massachusetts Council of Const. Employers,* 103 S. Ct. 1042, 1044 (1983); *Reeves, Inc. v. Stake,* 447 U.S. 429, 436, 439 (1980). The United States Supreme Court has, therefore, on several occasions held a state's participation in the market place as a competitor to be shielded from the Commerce Clause. *See, e.g., White,* 103

S.Ct. at 1048 (contracting for construction of public projects); *Reeves*, 447 U.S. at 440 (selling of cement); *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794, 809-810 (1976) (recycling of automobiles).

Yet in the case at bar, California's role cannot be said to be one of a market participant. The State owns and controls tidelands and submerged lands in its sovereign capacity. *See Bonelli Cattle Co. v. Arizona*, 414 U.S. 313, 320 (1973); *Shively v. Bowlby*, 152 U.S. 1, 58 (1894); *California v. United States*, 512 F. Supp. 36, 40 (N.D. Cal. 1981) (citing *Illinois Central R.R. v. Illinois*, 146 U.S. 387 (1892)). Although some of the lands are in the possession of local State entities or private interests, this does not mean that California becomes one of many competitors. The permanency of plaintiffs' facilities does not permit them to "shop around". There is no other competitor to which they can go for the rental of the required strip of California coastline. The Commission has a complete monopoly over the sites used by the oil companies. The companies have no choice but to renew their leases despite the volumetric rate, as the oil, gas and petroleum-derived products cannot be transported to plaintiffs facilities without traversing the state-owned lands. This control over the channels of interstate commerce permits the State to erect substantial impediments to the free flow of commerce. We therefore reject the State's contention that its leasing activities are not subject to Commerce Clause scrutiny.

B. *Volumetric Rate*

Plaintiffs do not dispute the State's right to the reasonable rental value of its property. They contend, however, that the computation of rent based on the volume of com-

modities passing through its pipelines bears no relationship to any benefit conferred by the State and that such a charge is unconstitutional.

The State argues that there is nothing unreasonable about its volumetric leases; they are a common rental mode used by other lessors. Moreover, it contends that the reasonableness of the volumetric rates have been determined in the related state court litigation; therefore, the parties are precluded by the doctrine of collateral estoppel from relitigating that issue.

A. *Reasonableness of the Volumetric Rates*

Our consideration of the reasonableness of the volumetric rates is not precluded by the state court litigation. The state proceedings addressed whether the throughput regulations were unreasonable, arbitrary and capricious "as an attempt to extract exorbitantly high charges for the use of state land. . . ." *Western Oil,* 105 Cal.App.3d at 560, 164 Cal.Rptr. at 471. This is a different inquiry from determining whether an assessment is reasonable for Commerce Clause purposes. The California court was not faced with the question whether the volumetric rates placed a burden on interstate commerce. Rather, they simply reviewed the Commission's promulgation to determine whether that agency was arbitrary, unreasonable, or capricious in adopting that rental mode. As the California Court of Appeals acknowledged, the State trial court was not requested to review the federal constitutional claims pending in federal court. *Id.* Moreover, under the abstention doctrine, a litigant should not be denied the right to have his claims fully litigated upon return to federal court. *England v. Louisiana State Bd. of Medical Examiners,* 375 U.S. 411, 421 (1964).

B. *Relation Between State Benefits Conferred and Volumetric Rates*

The district court below held that because the throughput charge is not regulatory in nature, its reasonableness is of no concern. The court then, however, went on to determine that there was no relation between the throughput charge and services and benefits provided by the State. This is the proper constitutional inquiry under the present facts, as our discussion will show.

Although the volumetric rates are designated as "rent" by the State, it is the practical effect of an exaction, not its label that is the focus of analysis under the Commerce Clause. *See, e.g., Commonwealth Edison Co. v. Montana,* 453 U.S. 609, 615 (1981); *Complete Auto Trasit, Inc. v. Brady,* 430 U.S. 274, 279 (1977); *Nippert v. Richmond,* 327 U.S. 416, 431 (1946). The volumetric charges are exacted specifically in return for the use of the coastal property. The present case therefore falls within the bounds of the Supreme Court cases that have reviewed "challenges to 'user' fees or 'taxes' that were designed and defended as a specific charge imposed by the State for the use of state-owned . . . facilities and services." *Montana,* 453 U.S. at 621. *See also St. Louis v. Western Union Tel. Co.,* 148 U.S. 92, 97 (1893) (rent "is not graduated by the amount of the business, nor . . . fixed for the privilege of doing business.").

California does have the right to exact compensation for conferring upon plaintiffs the right to use the real estate in question. *Id.* at 99. Further, the charges need only be a fair, not an exact approximation of the use of the land. *Evansville-Vanderburgh Airport Auth. Dist. v. Delta Airlines, Inc.,* 405 U.S. 707, 716-17 (1972). Yet these "user"

charges cannot be disproportionate to the benefits conferred by the State. *Montana*, 453 U.S. at 622 n.12; *Vanderburgh*, 405 U.S. at 714.

In applying the above principles to the case at bar, we find that the throughput charge is not directed toward compensating the State for the use of the land and violates the Commerce Clause. It is undisputed that the lands leased to plaintiffs are unimproved and that no services or facilities are provided by the State in conjunction with the lease. Plaintiffs must perform all operations that are required to make use of the land, such as dredging operations and installation and maintenance of the pipeline system. While under the pre-1976 leasing system, there was a correlation between the annual rental and the land's appraised value, a similar correlation is lacking under the present mode. Payments to the State now vary depending on the volume of petroleum substances travelling in interstate commerce, not on the "wear and tear" from use of the land. The United States Supreme Court has held a similar "compensating" charge to be violative of the Commerce Clause, because it was proportioned solely to the earning capacity of a vehicle, not the wear and tear caused by the vehicle incident to use of the state highways. *Interstate Transit, Inc. v. Lindsay*, 283 U.S. 183, 190 (1931). In that case, as in the case at bar, there was no sufficient relation between the measure employed and the extent of the use of the state property. *Id. See also Vanderburgh*, 405 U.S. at 714 (charge on state-provided facility must be designed to help defray its cost) (citing *Lindsay*); *McCarroll v. Dixie Greyhound Lines*, 309 U.S. 176, 180 (1940) (toll on amount of gasoline over 20 gallons in carrier's tank in return for road use invalidated).

The volumetric rates are also not justifiable as a means of compensating the State for environmental damage caused by the flow of plaintiffs' petroleum substances over the tide and submerged lands. Under both their leases and various state statutes, plaintiffs are held accountable for environmental damage resulting from their operations. The leases provide for the posting of a surety bond, the acquisition of public liability insurance for property damage, and requires plaintiffs to have an oil spill contingency plan. State statutes, in turn, provide for oil spill contingency plans and civil liability for environmental damage. *See, e.g.*, Cal. Gov't Code § 8574; Cal. Harb. & Nav. Code § 151; Cal. Water Code § 13350. It is also noteworthy that the administrative provisions do not require throughput charges to be related to services or facilities provided. *See* Cal. Admin. Code § 2005.

We are of the opinion that the volumetric rates are a disguised revenue raising measure. The rates do not reflect the value to the State of its land, but the maximum amount of revenue California can extract from interstate commerce by utilizing its strategic geographic position. There is no correlation between benefits conferred by the State and the throughput charges. We therefore hold that the charges impose an undue burden on interstate commerce and are violative of the Commerce Clause .

III. IMPORT-EXPORT CLAUSE

One of the major defects in the Articles of Confederation, and an impetus for the Constitutional Convention of 1787, was that the Articles allowed individual states to burden commerce among themselves and with foreign countries. *Michelin Tire Corp. v. Wages*, 423 U.S. 276, 283 (1976);

see also 1 W. Crosskey, *Politics and the Constitution in the History of the United States,* 295-323 (1953). "Before 1787 it was commonplace for seaboard States with port facilities to derive revenue to defray the costs of state and local governments by imposing taxes on imported goods destined for customers in other States." *Michelin* at 283. The founding fathers sought to limit state power to tax foreign commerce by absolute proscription announced in Article I, § 10, cl. 2 of the Constitution: "No State shall, without the Consent of Congress, lay any Imposts or Duties on Imports or Exports, except what may be absolutely necessary for executing its inspection Laws . . . ."

The term "impost or duty" is not self-defining, however, and not every state assessment that burdens foreign commerce is prohibited by the Clause. Although the constitution forbids the states from exploiting their position to the detriment of foreign commerce, they are entitled to compensation for services or property they provide. *Michelin Tire Corp. v. Wages,* 423 U.S. 276, 286-94 (1976); *Cooley v. Board of Wardens,* 53 U.S. (12 How.) 299, 315-20 (1851). In recent cases, the Supreme Court has focused the Import-Export analysis on whether a challenged exaction offends the policy considerations that underlie the Clause. *Department of Revenue v. Ass'n. of Washington Stevedoring Cos.,* 435 U.S. 734, 752-53 (1978); *Michelin,* 423 U.S. at 285-86. These policies are:

> [T]he Federal Government must speak with one voice when regulating commercial relations with foreign governments, and tariffs, which might affect foreign relations, could not be implemented by the States consistently with that exclusive power; import revenues were to be the major source of revenue of the Federal Government and should not be diverted to the

> States; and harmony among the States might be disturbed unless seaboard States, with their crucial ports of entry, were prohibited from levying taxes on citizens of other States by taxing goods merely flowing through their ports to the other States not situated as favorably geographically.

Id. (footnotes omitted).

We focus our analysis on the third Import-Export policy, namely whether the volumetric rates disturb the harmony among the States. The Supreme Court has held that such harmony is not disturbed if a coastal jurisdiction "receive[s] compensation only for services and protection extended to the imports." *Stevedoring,* 435 U.S. at 753. The High Court has, therefore, upheld a nondiscriminatory ad valorem property tax on imported tires stored in a Georgia warehouse, because the tax was the *quid pro quo* for benefits actually conferred by the state. *Michelin,* 423 U.S. at 288-90.

As our analysis under the Commerce Clause has shown, there is no correlation between the volumetric rates and benefits conferred by the State as required by *Michelin.*[2] We therefore come to the inevitable conclusion that the volumetric rates are not exacted in return for the use of the tide and submerged lands, but as "a form of tribute . . . to the disadvantage of the other States." *Michelin* at 286. California is exploiting its favorable geographic situation to exact a transit fee from the goods in question. It is "levying . . . on citizens of other States by taxing goods

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[2] "[T]he desire (under the third Import-Export policy) to prevent interstate rivalry and friction does not vary significantly from the primary purpose of the Commerce Clause." *Stevedoring,* 435 U.S. at 754.

merely flowing through their ports to the other states not situated as favorably geographically." *Id.* 285-86.

In calculating the value of the leaseholds, therefore, California cannot be permitted to rely on a rental formula that exploits its control over the crucial tidelands. "[A]s it cannot be done directly, it could hardly be a just and sound construction of the constitution which would enable a State to accomplish precisely the same thing under another name, and in a different form." *License Cases,* 46 U.S. (5 How.) 504, 576 (1847).

We also note that although the state regulations do not, by their terms, single out imported goods for assessment, this is the inevitable result. As previously stated, up to ninety-five of the crude oil entering California was in foreign commerce, and the evidence suggests that this estimate could have been higher. A charge that is nondiscriminatory on its face may well have the effect of discriminating against foreign goods, and the Supreme Court has made clear that it is "[n]ot the tax in a vacuum of words, but its practical consequences for the doing of interstate commerce in applications to concrete facts [that] are our concern." *Nippert,* 327 U.S. at 431.

IV. CONCLUSION

Today we hold that the volumetric throughput charge used by the California Lands Commission in the rental of tide and submerged lands is unconstitutional under the Commerce Clause and the Import-Export Clause. Our holding is not, however, to be understood as invalidating all volumetric leases. We recognize that the volumetric rate must be judged by its result, not its formula. *Vanderburgh* at 716.

AFFIRMED.

Appendix B

In the United States Court of Appeals
For the Ninth Circuit

No. 82-4261
D.C. No. Civ. S-76-513

Western Oil and Gas Association, et al.,
Plaintiffs-Appellees,

vs.

Kenneth Cory, et al.,
Defendants-Appellants

[Filed Feb. 29, 1984]

ORDER AMENDING OPINION

Before: TANG and ALARCON, Circuit Judges, and TAYLOR,* District Judge.

The opinion is hereby amended and the cite to *Bonelli Cattle Co. v. Arizona,* 414 U.S. 313 (1973) on page 202 of the slip opinion is deleted.

*Honorable Fred M. Taylor, District Judge for the District of Idaho, sitting by designation.

Appendix C

United States District Court
for the
Eastern District of California

Civil Action File No. 76-513 PCW

Western Oil and Gas Association, et al

vs.

Kenneth Cory, et al

[Filed Mar. 30, 1982]

JUDGMENT

This action came on for (hearing) before the Court, Honorable PHILIP C. WILKINS, United States District Judge, presiding, and the issues having been duly (heard) and a decision having been duly rendered,

It is Ordered and Adjudged that Judgment be and is hereby entered against Plaintiffs and in favor of Defendants on Plaintiff's Second Claim on grounds of res judicata.

Dated at Sacramento, California, this 30th day of March, 1982.

James R. Grindstaff
Clerk of Court

[Entered Mar. 30, 1982]

Appendix D

United States District Court
for the
Eastern District of California

Civil Action File No. CR S-76-513 PCW

Western Oil & Gas Association, et al

vs.

Kenneth Cory, et al

[Filed April 16, 1982]

AMENDED JUDGMENT

This action came on for (hearing) before the Court, Honorable PHILIP C. WILKINS, United States District Judge, presiding, and the issues having been duly (heard) and a decision having been duly rendered,

It is Ordered and Adjudged that Judgment be and is hereby ENTERED pursuant to the terms and conditions of the Court's Memorandum and Order filed April 15, 1982, a certified copy of which is attached hereto and incorporated herein by reference.

Dated at Sacramento, California, this 16th day of April, 1982.

James R. Grindstaff
Clerk of Court

[Entered April 16, 1982]

In the United States District Court
For the Eastern District of California

Civ. No. S-76-513 PCW

Western Oil and Gas
Association, et al.,
Plaintiffs,

v.

Kenneth Cory, et al.,
Defendants.

[Filed April 15, 1982]

AMENDED MEMORANDUM AND ORDER

The plaintiffs in this action are several oil companies and their trade organization. Defendants are the California State Lands Commission, its chairman, and two former members of the Commission [hereinafter SLC]. The SLC has exclusive jurisdiction over all tidelands and submerged lands owned by the State of California. It has power to lease such lands upon terms and conditions it deems to be in the best interests of the State. The SLC is authorized to promulgate rules and regulations to this effect. This action challenges the constitutional validity of one such regulation.

Plaintiffs own several oil and gas processing plants located on or near the coast of California. The amount of capital invested in these facilities is substantial. Petroleum substances must enter or depart from these facilities through a system of pipelines. Due to the physical and practical immobility of plaintiffs' processing plants, the pipelines must traverse tidal and submerged lands owned

by the State. Up to ninety-five percent (95%) of the petroleum substances entering the facilities are of foreign origin. From forty-six to ninety-eight percent (46-98%) of the petroleum products leaving the facilities are channeled into interstate and foreign commerce. These products remain in such commerce until they reach the ultimate consumer. *See, e.g., Maryland v. Louisiana,* 101 S.Ct. 2114, 2134 (1981). Plaintiffs lease from the State the tidal and submerged lands over which their pipelines must pass. The lands are unimproved, and the State provides no services or facilities to the lessees. Accordingly, plaintiffs must perform their own dredging operations, install their own pipelines, maintain their own pipeline systems, and perform any other operations necessary to make effective use of the lands. In addition, plaintiffs are held accountable both under the terms of their leases and by various state statutes for any environmental damage resulting from their operations. *See, e.g.,* Harbors & Navigation Code § 151; Government Code § 8574.1 *et seq.*

Prior to the commencement of this litigation, the SLC leased these lands at an annual rate based on 6% of the appraised value of the land. In 1975, the SLC decided to reconsider the manner in which rent was determined. In 1976, after extensive public hearings, the SLC promulgated the following regulation, which is the subject of this lawsuit.

> (2) Industrial Use: The rental may be based on eight percent (8%) per annum of the appraised value of leased land together with 1½ cents per diameter inch per lineal foot for pipelines and conduits within the leased premises; and/or an annual rental, with a specified minimum, based upon the volume of commod-

ities passing over State land. The minimum rental under either of these alternatives shall not be less than $550 per anum.

(3) Right of Way Use: Eight percent (8%) per annum of the appraised land value, together with damages, if any; and/or for pipelines and conduits, 1½ cents per diameter inch per lineal foot per annum, or, in lieu of either of the foregoing, an annual rental, with a specified minimum, based upon the volume of commodities passing over State land. The minimum rental under any of the above alternatives shall not be less than $550 per annum.

2 Cal. Admin. Code §§ 2005(b)(2) and 2005(b)(3).

In determining which rental assessment allowed by these subsections would best further the State's interests, the SLC must consider environmental factors, revenue potential, competitive effects, value assessment data, and other facts which the SLC finds to be relevant. *See* 2 Cal. Admin. Code § 2005(h). In each instance since the above-quoted provisions were adopted, upon renewal or assignment of a plaintiff's lease, the SLC has appraised the land, and has set a minimum rental of eight percent (8%) of the appraised value. Pursuant to the challenged Administrative Code provisions, however, the SLC has also imposed an additional charge at a progressive rate based *solely* on the volume of commodities passing over the leased lands, including commodities in interstate and foreign commerce. This charge is not based on the value of the commodities upon entering or exiting plaintiffs' facilities. This additional payment is referred to as a "volumetric throughput charge." As a result of this additional charge, the plaintiffs now pay up to approximately thirty percent (30%) of the appraised value of the leased lands as rental to the State.

On September 27, 1976, plaintiffs filed this action challenging the validity of California Administrative Code § 2005 on various state and federal grounds. Jurisdiction is predicated upon 28 U.S.C. § 1331. In 1977, plaintiffs moved for summary judgment without success and the Court stayed the action to allow state law issues to be litigated in state court. Plaintiffs subsequently filed suit in Sacramento County Superior Court and reserved the federal constitutional grounds for decision in this Court under the doctrine of *England v. Louisiana State Bd. of Med. Examiners,* 84 S.Ct. 461 (1964). The Superior Court upheld the Administrative Code provision on state law grounds, and the decision was affirmed on appeal. *See Western Oil & Gas Ass'n v. State Lands Commission,* 103 Cal. App. 3d 554 (3d Dist. 1980), *hearing denied,* 3 Civ. 18577 (Cal. S.Ct. July 2, 1980). The parties then returned to this Court with cross-motions for summary judgment. Oral arguments were heard on February 2, 1981, in this Court, the Honorable Philip C. Wilkins, presiding. After the hearing the parties submitted additional written arguments, the last of which was filed with the Court on July 29, 1981. The Court has considered all of the written and oral arguments of the parties and the exhibits filed in this action. Summary judgment is appropriate as the material facts are not in dispute.

Plaintiffs' challenge to the volumetric throughput charge is based upon three distinct but interrelated provisions of the Federal Constitution. Article I, Section 8, Clause 3 provides in pertinent part that "The Congress shall have power . . . to regulate Commerce with foreign Nations, and among the several States . . ." (hereinafter Commerce Clause). Article I, Section 10, Clause 2 provides that "No State shall, without the Consent of Congress, lay any

Imposts or Duties on Imports or Exports, except what may be absolutely necessary for executing its inspection Laws; . . . " (hereinafter Import-Export Clause). Finally, Clause 3 of the latter article and section reads as follows: "No State shall, without the Consent of Congress, lay any Duty of Tonnage, . . ." (hereinafter Duty of Tonnage Clause).

These constitutional provisions were designed to promote and ensure harmony both amongst the several states, and between the states and the federal government. Power to control commerce between the states was reserved to the federal government to protect interstate movement of goods from local trade barriers and thus to prevent interstate friction likely to result from retaliatory measures. *See H.P. Hood & Sons v. DuMond,* 69 S.Ct. 657, 665 (1949). In addition, the states were prohibited from levying "imposts or duties" on imports or exports in order to permit uniform federal regulation of foreign relations, to protect federal revenues derived from imports, and to maintain harmony among the inland states and the seaboard states. *See Washington Revenue Department v. Ass'n of Washington Stevedoring Companies,* 98 S.Ct. 1388, 1405 (1978) (Powell, J., concurring); *see also, Youngstown Sheet & Tube Co. v. Bowers,* 79 S.Ct. 383, 395 (1959) (Frankfurter, J., dissenting). Since this prohibition could be nullified by charging commercial vessels for the privilege of access to the ports of a state, the states were further prohibited from leving any "duty of tonnage" having such an effect. *See Clyde Mallory Lines v. Alabama,* 56 S.Ct. 194, 196 (1935). In reliance upon this constitutional scheme, plaintiffs argue that the volumetric throughput charge is the type of evil that the clauses, collectively, were designed to prevent.

Initially, the Court notes that the SLC has advanced several arguments concerning the reasonableness of the throughput charge. *See* Defendants' Opening Brief, pp. 20-29, *see also* Defendants' Reply Brief, pp. 3-7. Consideration of whether a charge is "rational" is of concern when Commerce Clause, equal protection or due process challenges are lodged against state regulatory activity. *See, e.g., Kassell v. Consolidated Freightways Corp.*, 101 S.Ct. 1309 (1981); *Minnesota v. Clover Leaf Creamery Co.*, 101 S.Ct. 715 (1981); *Cities Services Gas Co. v. Peerless Oil & Gas Co.*, 71 S.Ct. 215 (1950). In the present case, however, the disputed throughput charge is not regulatory in nature, nor has either party attempted to characterize it in such a fashion. Thus, the "reasonableness" of the throughput charge is of no particular concern to the Court as this action has been framed.

It is undisputed that the State leases unimproved lands and furnishes no services or facilities to the plaintiffs, nor is the State obligated to do so. There is no language in the administrative provision requiring the throughput charge to be related to services or facilities provided. *See* Cal. Admin. Code § 2005. Thus, there is no argument that the throughput charge is exacted as compensation for the provision of services or facilities. *Cf., Washington Revenue Department v. Ass'n of Washington Stevedoring Companies, supra; Clyde Mallory Lines v. Alabama, supra.* Nor is it argued that the charge is based on the value of the commodities involved. *Cf., Commonwealth Edison Co., v. Montana*, 101 S.Ct. 2946 (1981) (variable rate coal severance tax based on value, energy content, and extraction method used). The SLC's primary argument has been that the use of a volumetric throughput charge does not implicate any

of the aforementioned constitutional provisions. The SLC has consistently argued that the State is acting in its "proprietary" capacity as a landowner in charging a "rental," rather than as a sovereign in assessing a tax, impost or duty. *See* Defendants' Opening Brief, pp. 12-33; *see also,* Defendants' Reply Brief, pp. 1-3. Thus, the SLC contends that this "proprietary activity" is outside the scope of the Commerce, Import-Export and Duty of Tonnage clauses. Accepting the SLC's characterization of the State's activity as true, however, it is also true that bold assertions of state proprietary power, in name or effect, are not impervious to constitutional attack. *See, e.g., City of St. Petersburg v. Alsup,* 238 F.2d 830 (5th Cir. 1956); *Haskell v. Cowham,* 187 F. 403 (8th Cir. 1911). In a few cases, the sovereign-proprietary distinction has been rejected altogether as a tenable basis for analysis. *See New York v. United States,* 66 S.Ct. 310, 312-314 (1946); *Massachusetts v. United States,* 98 S.Ct. 1153, 1162 & n.14 (1978).

The recent Commerce Clause decisions in which state assertions of proprietary power *were* upheld involved state competition in the marketplace for fungible goods. *See, e.g. Reeves v. Stake,* 100 S.Ct. 2271 (1980); *Hughes v. Alexandria Scrap Corp.,* 96 S.Ct. 2488 (1976); *American Yearbook Co. v. Askew,* 339 F. Supp. 719 (M.D.Fla. 1972). A comparable specific immunity for state participation in the marketplace, however, is not appropriate herein since there is no analogous competitive marketplace involved in this case. "Moreover, any general immunity for proprietary action could well exacerbate trade barriers of serious and growing significance." L. Tribe, *American Constitutional Law* 336-337 (1978).

A fundamental purpose of the Commerce, Import-Export and Duty of Tonnage clauses, collectively, is to prevent interstate friction that results from a state using its geographic location to erect trade barriers. The Court has determined that the State's imposition of the throughput charge is such a trade barrier and constitutes " . . . the kind of action with which the [clauses are] concerned." *Hughes v. Alexandria Scrap Corp., supra.* Because the volumetric throughput charge places a burden on interstate and foreign commerce that cannot be justified under the facts of this case, the Court finds that the SLC's assessment of "rent" based on the volume of commodities in interstate and foreign commerce passing over the State's tidal and submerged lands is invalid. Accordingly,

IT IS HEREBY ORDERED that plaintiffs' motion for summary judgment be, and the same hereby is, GRANTED.

IT IS FURTHER ORDERED that defendants' motion for summary judgment be, and the same hereby is, GRANTED as to plaintiffs' second claim on the ground of res judicata. *See* Order of March 30, 1982. In all other respects, defendants' motion for summary judgment is DENIED.

IT IS FURTHER ORDERED that defendants are hereby enjoined from assessing and collecting rent based on the volume of commodities in interstate and foreign commerce passing over tidal and submerged lands in reliance upon California Administrative Code §§ 2005(b)(2) and 2005(b)(3). This amended memorandum and order shall serve as the Court's findings of fact and conclusions of law in support of this injunction. F.R.Civ.P. 52(a) and 65(d).

IT IS FURTHER ORDERED that the Clerk of the Court enter an amended judgment in conformity with the foregoing.

DATED: April 14, 1982

/s/ Philip P. Wilkins
United States District Judge

Appendix E

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 82-4261
DC# Civ. S-76-513

WESTERN OIL and GAS ASSOCIATION, ET AL.,
Plaintiffs-Appellees,

vs.

KENNETH CORY, ET AL.,
Defendants-Appellants,

[Filed April 6, 1984]

ORDER

Before: TANG and ALARCON, Circuit Judges, and TAYLOR,* District Judge.

The panel as constituted above has voted to deny the petition for rehearing and to reject the suggestion for rehearing en banc.

The full court has been advised of the suggestion for rehearing en banc, and no judge of the court has requested a vote on the suggestion for rehearing en banc. Fed. R. App. P. 35(b).

The petition for rehearing is denied and the suggestion for rehearing en banc is rejected.

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*Honorable Fred M. Taylor, District Judge for the District of Idaho, sitting by designation.

Appendix F

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 82-4261
DC No. Civ. S-76-513

WESTERN OIL & GAS ASSOCIATION, et al.,
Plaintiffs-Appellees,

v.

KENNETH CORY, et al.,
Defendants-Appellants.

[Filed April 10, 1984]

NOTICE OF APPEAL TO THE SUPREME COURT
OF THE UNITED STATES

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IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 82-4261
DC No. Civ. S-76-513

WESTERN OIL & GAS ASSOCIATION, et al.,
Plaintiffs-Appellees,

v.

KENNETH CORY, et al.,
Defendants-Appellants.

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

Notice is hereby given that Kenneth Cory, Leo T. McCarthy, and Jesse R. Huff, members of the California State Lands Commission, hereby appeal to the Supreme Court of the United States from the judgment of the United States Court of Appeals for the Ninth Circuit, entered in this action on January 13, 1984. The Court of Appeals denied appellants' petition for rehearing on April 6, 1984.

This appeal is taken pursuant to 28 United States Code section 1254(2).

DATED: April 10, 1984

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N. Gregory Taylor
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Appendix G

CURRENT SECTIONS 1900, 2000, 2002, 2003, and 2004 OF TITLE 2, CALIFORNIA ADMINISTRATIVE CODE

Article 1. General Provisions

1900. Definitions.

The following definitions shall apply to this Chapter unless otherwise providcd.

(a) The term "applicant" includes any person who files an application under these regulations.

(b) The term "person" includes any individual, firm, partnership, business entity, business trust, association, corporation, or governmental entity or agency.

(c) The term "lease" includes a permit, right-of-way, easement, license, compensatory agreement, or other entitlement of use.

(d) The term "structure" means any manmade construction.

(e) The term "submerged lands" means the area lying below the elevation of ordinary low water in the beds of all tidal and nontidal navigable waters.

(f) The term "tidelands" means the area lying between the elevations of ordinary low water and ordinary high water on lands subject to tidal action.

(g) The term "uplands" shall mean lands bordering on navigable waterways.

(h) The term "school lands" refers to all Sections 16 and 36 granted to the State for the benefit of common schools by Chapter 145 of the Federal Statutes of 1853.

(i) The term "lieu or indemnity lands" refers to those lands acquired by the State in place of school lands it previously acquired or school lands to which it did not receive title because they were either mineral in character, had not been sectionalized, or were subject to prior established rights.

(j) The terms "merchandise", "product" and "commodity" are interchangeable and shall include, goods, wares, chattels, personal property of every description, cargo, freight, mail, vessel's stores and supplies, articles, matter and material.

* * * *

Article 2. Leasing or Other Use of Public Lands

2000. General.

(a) This article applies to the leasing of all lands under the Commission's jurisdiction for all surface uses except the exploration for or extraction of natural resources including minerals, oil, gas or other hydrocarbons, or geothermal resources or any other natural resources, excluding timber.

(b) Leases or permits may be issued to qualified applicants and the Commission shall have broad discretion in all aspects of leasing including category of lease or permit and which use, method or amount of rental is most appropriate, whether competitive bidding should be used in awarding a lease, what term should apply, how rental should be adjusted during the term, whether bonding and insurance should be required and in what amounts, whether an applicant is "qualified", etc. based on what it deems to be in the best interest of the State.

(c) Leases or permits for tide or submerged lands shall generally only be issued to riparian or littoral upland owners or use right holders, provided however that such leases or permits may be granted to the best qualified applicant irrespective of riparian or littoral status.

(d) Leases or permits for school, lieu or indemnity lands shall be for value or value enhancement purposes.

* * * *

2002. Categories of Leases or Permits.

(a) General Lease: Uses may include the following:

(1) Commercial: Income producing uses such as marinas, restaurants, clubhouses, recreation piers or facilities, docks, moorings, buoys, helicopter pads, decks or gas service facilities.

(2) Industrial: Uses such as oil terminals, piers, wharves, warehouses, stowage sites, moorings, dolphins and islands; together with necessary appurtenances.

(3) Right of Way: Uses such as roadways, power lines, pipelines or outfall lines, except when used only as necessary appurtenances.

(b) General Permit: Uses may include the following:

(1) Public agency uses such as public roads, bridges, recreation areas or wildlife refuges having a statewide public benefit;

(2) Public Resources Code Section 6321 protective structures such as groins, jetties, sea walls, breakwaters and bulkheads;

(3) Non income producing uses such as piers, buoys, floats, boathouses, docks, waterski facilities, and camp-

sites not qualifying for a private recreational pier permit under 2002(f). Other uses may include campsites, cabins, dwellings, arks, houseboats, or boathouses provided that when such uses are located on sovereign lands that such uses are not found to be inconsistent with public trust needs.

(c) Grazing Lease: Use includes the feeding of livestock on forage.

(d) Agricultural Lease: Uses may include farming, silviculture and horticulture.

(e) Forest Management Agreement: Uses may include reforestation, improvement of timber growth and soil productivity, vegetation control, reduction of fire and erosion hazards, insect or disease control or any other use that enhances the value of lands subject to the agreement.

(f) Private Recreational Pier Permit: Use is limited to any fixed facility for the docking or mooring of boats constructed for the use of the littoral landowner, as specified in Public Resources Code Section 6503.5, and does not include swimming floats or platforms, sun decks, swim areas, fishing platforms, residential, recreational dressing, storage or eating facilities or areas attached or adjacent to recreational piers, or any other facilities not constructed for the docking or mooring of boats.

(g) Salvage Permit: Use includes the salvage of all abandoned property over and upon ungranted tide and submerged lands of the State which property belongs to the State and is under the Commission's jurisdiction pursuant to Public Resources Code Section 6309. The Commission may retain or sell any or all salvaged property or may allow the permit applicant to retain it.

2003. Rental.

(a) Rental for the various categories of use shall be generally as follows:

(1) Commercial Use: An annual rental based on any one or combination of the following rental methods, with a minimum rental of $250:

(A) A percentage of annual gross income (the percentage being based on an analysis of the market for like uses and other relevant factors);

(B) 9% of the appraised value of the leased land;

(C) The volume of commodities passing over the lease premises.

(2) Industrial Use: An annual rental based on any one or combination of the following rental methods with a minimum rental of $250:

(A) 9% of the appraised value of the leased land together with 2¢ per diameter inch per lineal foot of pipelines and conduits on the leased premises;

(B) The volume of commodities passing over the lease premises.

(3) Right-of-Way Use: An annual rental based on any one or combination of the following rental methods with a minimum rental of $100:

(A) 9% of the appraised value of the leased lands, together with compensation for any damage caused to such lands;

(B) 2¢ per diameter inch per lineal foot;

(C) The volume of commodities passing over the leased premises.

(4) General Permits: Annual rental shall be based on 9% of the appraised value of the leased lands with a minimum rental of $50.

(A) No rental shall be charged for public agency use of tide and submerged lands if the Commission at its sole discretion, determines that a statewide public benefit accrues from such use.

(B) Monetary rental for Public Resources Code Section 6321 protective structures may be waived if the Commission determines that a public benefit accrues from the installation of such structures.

(5) Private Recreational Pier Permits: Pursuant to Public Resources Code Section 6503.5 a rent free permit shall be used to those applicants demonstrating their qualifications under that section as implemented by 2002(f).

(6) Grazing: An annual rental based on appraised value for the intended use.

(7) Agricultural: An annual rental based on any one or a combination of the following rental methods with a minimum rental of $250:

(A) A percentage of annual gross income (the percentage being based on analysis of the market for like uses and other relevant factors);

(B) 9% of appraised value of the leased lands.

(8) Forest Management Agreements: Rental shall constitute enhancement of the land's value resulting from the use.

(9) Salvage Permit Rental shall be as follows:

(A) A rental of $25.00 per annum per acre, computed on a whole or fractional basis, for the total acreage of the permit area; and

(B) 25% of the net salvage value up to $25,000 and 50% of all such value over that amount for all salvaged property the salvor is permitted to retain; or

(C) The net salvage value of any property the State retains less any rental to which it is entitled; and

(D) Such other consideration as may be deemed by the Commission to be in the best interest of the State.

(b) The following factors shall be considered by the Commission in determining which rental method should apply:

(1) The amount of rental the State would receive under various rental methods;

(2) Whether relevant, reliable and comparable data is available concerning the value of the land proposed to be leased;

(3) Whether a particular method or amount of rental would effectively cause an applicant to use more competitive substitute land or to abandon its project altogether;

(4) Whether the land proposed to be leased has been classified as environmentally significant pursuant to Public Resources Code Section 6371.

(5) The monetary value of actual or potential environmental damage anticipated from an applicant's proposed use to the extent such damage is quantifiable;

(6) Other factors relating to the appropriateness of the proposed rental method.

(c) The following limitations shall apply to rental based on the volume of commodities passing over State lands:

(1) Rental shall not be imposed more than once for the identical commodity passing over the same State land if the ownership of that commodity has not changed.

(2) The rental rate for a right-of-way for passage of a commodity across State lands shall be made proportional to the percentage of the total length of the pipeline or conduit that such right-of-way comprises. For the purposes of this section, the total length of a pipeline or conduit shall be the length of the pipeline or conduit between two facilities, uninterrupted by another facility. "Facility" includes terminal, production, storage, refining, manufacturing, processing, mixing or intermixing facilities.

(d) Rental adjustment during the lease term shall be provided for as appropriate.

2004. Term.

(a) The term for leases and permits including any optional renewal periods shall be no longer than necessary to accomplish the intended use or purpose.

(b) The term shall be limited according to standard commercial practices with maximum terms as follows:

(1) General Lease General Permit Forest Management Agreement	49 years
(2) Agricultural Lease	25 years
(3) Grazing Lease Private Recreational Pier Permit General Permit Recreational Use	10 years
(4) Salvage Permit	1 year but extendable for one additional year.

Appendix H

FORMER SECTIONS 2006 AND 2007 OF TITLE 2, CALIFORNIA ADMINISTRATIVE CODE*

2006. Payment of Rentals.

(a) Amount: Leases executed pursuant to this Article shall contain provisions for the payment of rental based upon the rates established by the following schedule in fixed sums, in sums based in whole or in part on gross income, volume or quantity of materials passing over State lands, or for such other consideration as, in the judgment of the Commission, may be in the best interests of the State.

(b) Rental Rate Schedule: The following rates shall apply to the classifications listed below:

(1) Commercial Leases: A percentage, as provided in Section 2007, of annual gross income, and/or 8% per annum of the appraised value of the leased land, with a $450 minimum annual rental.

(2) Industrial Lease: Eight percent per annum of the appraised value of leased land together with 1½ cents per diameter inch per lineal foot for pipelines and conduits within the leased premises; or, an annual rental, with a specified minimum, based upon the volume of commodities passing over State land. The minimum rental under either of these alternative rentals shall be not less than $450 per annum.

(3) Use Permits: A fixed rental of $75 per annum for areas less than 1,000 square feet, and $100 per annum for areas of 1,000 square feet to 3,000 square feet.

(4) Grazing and Agricultural Leases: Rental based on appraisal for the use intended.

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*Cal. Admin. Register 76, No. 18, 6-1-76.

(5) Public Agency Leases: Leases of State land to public agencies shall provide for monetary rental, unless the Commission determines that a state-wide public benefit accrues, equal to that prescribed for other leases and permits according to intended land use and as set forth in this section.

(6) Public Agency Permits: The consideration for this type permit shall be the state-wide public benefit, use, health or safety: provided, that it shall be incumbent upon the applicant to show such state-wide applicability; otherwise a Public Agency Lease with monetary consideration shall apply.

(7) Right of Way: Eight percent (8%) per annum of the appraised land value, together with damages if any; or alternatively, for pipelines and conduits, 1½ cents per diameter inch per lineal foot per annum, or, in lieu of either of the foregoing, an annual rental, with a specified minimum, based upon the volume of commodities passing over State land. The minimum rental under any of the above alternatives shall not be less than $100 per annum.

(8) Protective Structure Permits: 8% of the appraised land value, however, with consideration for state-wide public benefits.

(9) Noncommercial Leases and Minor Commercial Leases: 8% of the appraised land value, with a $225 minimum annual rental.

(c) Rentals Subject to Law: In cases where leases are exempted from rental by law or if rates are particularly controlled or established by law, rental charges shall be governed by such law.

(d) Other Consideration: The Commission reserves the right to grant leases for such other considerations as may be deemed by the Commission to be in the best interests of the State.

(e) Review: Leases may contain provisions which provide for review of rental rates, at intervals as the Commission may require. Such leases shall provide that any new rental rate shall be effective upon reasonable notice to the lessee as more specifically set forth in the lease.

(f) Time of Payment: The first year's rental shall be paid in advance; rentals for following years shall be paid not later than 15 days after the beginning of each such following year, provided, however, that rental under leases requiring computations to ascertain the rental rate may be paid in whole or in part at other times as specified in the lease. Where the annual rental for any period is $225 or less, the total rental for such period or for 5 years, whichever is less, shall be paid in advance.

(g) Interest on Retroactive Payments: In the event that, for purposes of lease renewal or extension, a lessee does not agree to an annual rental, as offered by the Commission at the expiration of the lease period, and the lessee remains in possession of the leased lands while continuing to pay interim rental until a firm rental is agreed upon by the parties, than at such time as lessee submits payment for any or all retroactive rentals, the lessee shall pay interest to the State on said retroactive payments at the legal rate in effect at the time of said retroactive payment.

(h) Selection Among Alternative Rentals for Industrial and Right of Way Leases: The following factors shall be considered by the Commission in determining which of the alternative rentals provided for industrial and right of way leases is in the best interests of the State;

(1) Whether the land to be leased has been classified as environmentally significant under Article 11 of this Division;

(2) The actual and potential environmental damage inhering in the lessee's proposed use of the land, and the extent to which such damage is quantifiable;

(3) The revenue that would accrue to the State under each alternative;

(4) Whether a particular rental rate would have the result, if imposed by the Commission, of compelling the use of substitute facilities by the prospective lessee.

(5) The availability, reliability, and applicability of comparable or related data concerning the value of the land to be leased;

(6) Such other factors as, in the opinion of the Commission, reasonably bear on the appropriateness of the rental to be charged.

2007. Percentage Rentals and Limitations on Rentals Based on Volume of Commodities. (a) Commercial leases may provide for the payment to the State by the lessee of a minimum flat rent based upon land value, and/or a reasonable percentage of gross receipts where the Commission finds it is in the best interests of the State.

(b) If the Commission determines that a rental based on the volume of commodities passing over State land is in the best interests of the State, the following limitations to such volume rentals shall apply:

(1) Rental shall not be imposed for passage of a commodity over State land if rental has already accrued on that identical commodity for passage over the same State land over which it is again passing, provided the commodity is still in the same ownership as upon the next preceding passage over said State land for which rental has accrued.

(2) The rental rates for rights of way shall be apportioned in the proportion that the length of the pipeline or other structure over State land bears to the total length of the subject pipeline or structure over the land of the State and other persons. "Subject pipeline or structure" is defined as the pipeline or structure by which the commodity is being transported on a route between two facilities, uninterrupted by another facility. "Facility" includes terminal, production facility, storage facility, refinery or other manufacturing or processing facility, or point at which the commodity is or may be intermixed with the same or a different commodity.